

**DEPARTMENT OF STATE REVENUE**

**LETTER OF FINDINGS NUMBER 04-20050041P  
TAX ADMINISTRATION (GROSS RETAIL AND USE TAX)—  
NEGLIGENCE PENALTIES FOR THE REPORTING PERIODS  
COVERING CALENDAR YEARS 2001-03**

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**ISSUES**

**I. Tax Administration—Negligence Penalties—Audit Deficiencies—Good Filing History**

Authority: IC §§ 6-8.1-5-1(b) and -10-2.1 (2004); 45 IAC §§ 15-5-3(b)(8) and -11-2 (2004)

**II. Tax Administration—Negligence Penalties—Audit Deficiencies—Ignorance of Law**

Authority: IC §§ 6-8.1-5-1(b) and -10-2.1 (2004); 45 IAC §§ 15-5-3(b)(8) and -11-2 (2004)

The taxpayer protests the Audit Division's proposed assessment of negligence penalties.

**STATEMENT OF FACTS**

The Department's Audit Division conducted a field audit of the taxpayer for the tax type and reporting periods set out in the heading of this Letter of Findings. As a result of the audit, the taxpayer incurred tax deficiencies. The Audit Division proposed assessing, and the taxpayer has protested only proposed assessment of, negligence penalties. The Department will provide additional information as needed.

**I. Tax Administration—Negligence Penalties—Audit Deficiencies—Good Filing History**

## DISCUSSION

### A. TAXPAYER'S ARGUMENT

The taxpayer submits that one reason the Department should waive the negligence penalties is that it is a “good corporate citizen” and files all of its returns on time.

### B. ANALYSIS

IC § 6-8.1-10-2.1 (2004) is the statute that authorizes the Department to impose a penalty for any negligence of a taxpayer in failing to comply with the tax laws that the Department administers. These taxes are listed in IC § 6-8.1-1-1 and include the gross retail and use tax. IC § 6-8.1-10-2.1(a)(3) states that “(a) [i]f a person: ... (3) [i]ncurs, upon examination by the department, a deficiency that is due to *negligence*; ... the person is subject to a penalty.” *Id.* (Emphasis and alterations added). The amount is set by IC § 6-8.1-10-2.1(b)(4), which states that “(b) [e]xcept as provided in subsection (g) [,] [not in issue here], the penalty described in subsection (a) is ten percent ... of: ... (4) the amount of deficiency as finally determined by the department[.]” *Id.* (Alterations added.) However, IC § 6-8.1-10-2.1(d) states that “[i]f a person subject to the penalty imposed under this section can show that the failure to...pay the deficiency determined by the department was due to *reasonable cause* and not due to willful neglect, the department shall waive the penalty.” *Id.* (Emphasis and alteration added).

Title 45 IAC § 15-11-2(b) states:

(b) “Negligence” on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's *carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence.* Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

*Id.* (Emphasis added.) The next subsection of the regulation sets out the standard of care a taxpayer must prove pursuant to IC § 6-8.1-10-2.1(e) to establish reasonable cause for failing to meet its tax compliance duties to the Department. Subsection (c) of 45 IAC § 15-11-2 reads in relevant part as follows:

(c) The department shall waive the negligence penalty imposed under IC 6-8.1-10-1 [sic][should read IC 6-8.1-10-2, repealed and re-enacted in 1991 as IC 6-8.1-10-2.1] if the taxpayer affirmatively establishes that the failure to...pay a deficiency was due to reasonable cause and not due to negligence. *In order to*

*establish reasonable cause, the taxpayer must demonstrate that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed under this section ....*

...

Reasonable cause is a fact sensitive question and thus will be dealt with according to the particular facts and circumstances of each case.

*Id.* (Emphasis and alterations added.)

Under IC § 6-8.1-5-1(b) (2004) and 45 IAC § 15-5-3(b)(8) (2004), the person against whom a proposed assessment is made has the burden of proving that it is wrong. That burden applies to abatement of penalty assessments, as well as substantive tax assessments. “A person who wishes to avoid the penalty imposed under [IC § 6-8.1-10-2.1(a) and (b)] must make an affirmative showing of all facts alleged as a reasonable cause for the person’s failure to file the return, pay the amount of tax shown on the person’s return, pay the deficiency, or timely remit tax held in trust[.]” IC § 6-8.1-10-2.1(e) (emphasis and alterations added). The burden of proof is not on the Department to show negligence, willful or otherwise, by, or the absence of reasonable cause for the actions or inaction of, a taxpayer.

The taxpayer’s argument is in effect that it exercised ordinary care and prudence in filing its returns with this Department, thereby implying that it had “reasonable cause,” as 45 IAC § 15-11-2(c) defines that term, for its incurring audit deficiencies. That argument does not support the taxpayer’s protest because it does not address the basis on which the negligence penalties were proposed against it. The taxpayer was not penalized by the Compliance Division under IC § 6-8.1-10-2.1(a)(1) or (2) for failing to file returns, for failing to file returns on time, or for failing to pay the full amount of tax shown on those returns. It was penalized by the Audit Division under IC § 6-8.1-10-2.1(a)(3) for “[i]ncur[ring], upon examination by the department, a deficiency that is due to negligence[.]” *Id.* (Alterations added.) The fact that the taxpayer filed its returns promptly and paid all the tax it reported has no tendency to prove that the present deficiencies, resulting from its omissions of tax from those returns, were incurred for reasonable cause. The taxpayer has therefore failed to sustain its burden of proof concerning the proposal of the negligence penalties to the extent it has based its protest on this ground.

### **FINDING**

The taxpayer's protest is denied to the extent it is based on this issue.

## **II. Tax Administration—Negligence Penalties—Audit Deficiencies—Ignorance of Law**

## **DISCUSSION**

### **A. TAXPAYER'S ARGUMENT**

The taxpayer failed to accrue and remit use tax on licenses for new software on which its licensors/vendors did not charge it gross retail (sales) tax. The taxpayer submits that the other reason the Department should waive the negligence penalties is that these failures were unintentional. The protest letter implies that the taxpayer did not previously know that such licenses were subject to sales and use tax.

### **B. ANALYSIS**

The taxpayer's argument is in effect that it did not know that it was liable for tax on the largest single category of retail transactions on which the Audit Division ultimately proposed to assess the audit deficiencies against it. The taxpayer thus has admitted that it was "ignorant of the listed tax laws, rules and/or regulations[,] which is treated as negligence." 45 IAC § 15-11-2(b) (alterations added). Such ignorance is not an exercise of "ordinary business care and prudence[,] *id.*(c) (alteration added), and therefore does not establish reasonable cause under IC § 6-8.1-10-2.1(d) and 45 IAC § 15-11-2(c) to waive the proposed negligence penalties.

## **FINDING**

The taxpayer's protest is denied.